SEC Advisory Committee on Small and Emerging Companies

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Overview

- In the US, being public creates opportunities and burdens of disclosure required by investors, exchanges and the SEC that are intended to provide for transparency and appropriate disclosure, with the goal of allowing for the allocation of capital in an efficient as well as predictable fashion.

- Current practice requires not only the registration of the company and continuous reporting requirements, but also the registration of each class of securities offered and sold.

- In certain jurisdictions with recognized securities markets, company registration and a much less burdensome process of registering any securities offering has shown to be workable.

Registration Requirement

- Offerings of securities generally require that a registration statement be filed prior to offering securities to the public and that the registration statement be declared “effective” prior to the actual sale of securities.

- Under the current registration structure, with the exception of certain registration statements available to the largest issuers, all registration statement are subject to the uncertainty of delays caused by the SEC review process. This uncertainty, when combined with the uncertainty inherent in the financial markets combine to weigh against doing certain registered offerings in lieu of unregistered offerings.

- Additionally, current requirements for securities registration follow a somewhat inconsistent approach when applied to seemingly similar companies and situations and may impose undue burden and delay in allowing companies to access capital in the most efficient manner vis-à-vis timing and cost.

S-1

- This form of registration statement is used by a domestic US entity to do an initial public offering and entails substantial disclosure by an issuer of all aspects of a company's business and financial condition. This form requires hundreds of hours of preparation as well as the involvement of attorneys and accountants, and is generally reviewed by the SEC in a lengthy process.

- It is often the seminal document that establishes a company's public reporting record upon which many other filings and disclosures spring. From a due diligence perspective, it is very often used by investors, analysts, competitors, and other industry participants to understand and assist in valuing an entity entering the public markets.

- Once public, companies, through 1934 Act filings such as 10Qs and Ks, 8-Ks, etc., disclose financial performance, changes in business lines and segments, competitive developments, etc. These various documents and the system of disclosure under EDGAR allow investors and analysts to follow a company and its progress, or lack thereof, in a chronologically ordered, searchable database of information that is easy to use.

S-1 (cont'd)

- Form S-1 is also used once a company is public to register securities sold in publicly marketed follow-on offerings as well as those sold through non-publicly marketed registered offerings and private placements of securities under various exemptions.

- This use of S-1 by public company that is fully reporting under the 1934 Act requires substantial preparation and cost by an issuer and is very redundant in that it requires re-disclosure of information already available through previous filings.

S-3

- This form of registration is eligible for use by a company once it has become public and seasoned for a while, and carries a substantially smaller burden in time and cost to issuers through allowing incorporation by reference of other previous SEC filings.

- Where available, this form has become the preferred means by which public companies register and offer securities.

- It may be used to register a broad range of types of securities, is effective for three years once declared effective, and can be used to register new issue securities, as well as to register existing outstanding securities of affiliates or other holders and is used to effectuate fully marketed public offerings, private offerings of registered securities and other recently developed capital markets products such as At-The-Market Offerings (“ATMs”).

- Until 2008, Form S-3 was only used by seasoned issuers with market values of public float in excess of $75 million, which substantially limited its use by the community of smaller public companies most in need of access to the capital markets to fund their businesses.

S-3 (cont'd)

- That situation was why in the not distant past, most capital raising by smaller public companies was in the form of private placement to institutional investors of heavily discounted restricted equity with warrant sweeteners and equity linked, structured convertibles that could be highly dilutive to existing shareholders. These securities, once placed, carried liquidity risk to the investors and in most cases required the issuer to register them on Form S-1 for resale under agreements providing for penalties if registration was delayed.

- When S-3 was made available more broadly a few years ago, the community of small capitalization companies was ready to breathe a sigh of relief at the prospect of having the substantial burden of having to rely on S-1 removed and broader use of S-3 made available.

- Despite widening the use of S-3 overall, several limitations, which do not appear to substantially improve investor protection were imposed that for the companies perhaps most in need of capital markets access, created a burden and substantially limited or prohibited the use of S-3.

- These limitations include restrictions of use of S-3 by many non-exchange listed companies and annual limits on securities issuances under S-3 by companies with public float of under $75 million.

S-3 (cont'd)

- An upshot of the above limitations is that while the general sentiment has been to facilitate better transparency and greater access to the capital markets, fully reporting smaller public companies in need of capital must still use PIPEs and offerings off of the far more burdensome S-1 to access the capital markets.

Suggested Changes

- Allow non-exchange listed companies with public float below $75 million to use S-3
- Change the “baby shelf” limit on annual issuance amounts for companies with a public float of below $75 million to a greater percentage of the outstanding shares
- Allow for the filing and immediate effectiveness of S-3 by a wider group of issuers by reducing the $750 million market value/WKSI test to a substantially lower amount ($100-$250 million), thus allowing for a much greater number of seasoned issuers to more timely access capital if the market is available
- Allow forward incorporation by reference of subsequent 1934 Act filings into S-1 for any issuer, thus substantially reducing the unnecessary redundancy and current burden inherent in S-1 resale registration statements